United States Department of Agriculture

Food and Nutrition Service

3101 Park Center Drive

Alexandria, VA 22302-1500

December 6, 2004

SUBJECT: WIC Final Policy Memorandum # 2005-1
Implementation of Certain WIC Vendor Provisions of P.L. 108-265

TO: Regional Directors
Supplemental Food Programs
All Regions

This policy memorandum concerns most of the provisions of the Child Nutrition and WIC Reauthorization Act of 2004, P.L. 108-265, impacting on retail vendors authorized by State agencies to provide supplemental food to participants in exchange for WIC food instruments. These provisions, all of which were effective on or before October 1, 2004, involve: 1) State agencies processing vendor applications outside of established timeframes; 2) State agencies allowing participants to receive supplemental food from any authorized vendor; 3) State agencies notifying vendors of violations; 4) vendors obtaining infant formula only from State agency lists of manufacturers or wholesalers, distributors, or retailers licensed by State authorities; 5) prohibiting State agencies from imposing costs on vendors related to Electronic Benefit Transfer systems; and, 6) State agencies enforcing restrictions on incentive items provided to participants by vendors for which more than 50 percent of annual food sales result from WIC sales. The policy memorandum also encourages State agencies to use vendor advisory panels for dialogue and collaboration with vendors, consistent with the House and Senate Reports on the reauthorization legislation.

Regulations formally implementing these statutory provisions will be forthcoming.

This policy memorandum does not address the vendor cost containment provisions of the reauthorization legislation concerning peer groups, competitive price requirements for vendor selection and allowable reimbursement levels. Guidance and regulations will be provided in the near future on these provisions. Also, a policy memorandum will be issued in the near future to assist State agencies in identifying vendors that derive more than 50 percent of annual food sales from the sale of WIC supplemental foods.

/s/
PATRICIA N. DANIELS
Director
Supplemental Food Programs Division

Attachment

PROCESSING VENDOR APPLICATIONS OUTSIDE ESTABLISHED TIMEFRAMES

Legislative Change: Section 203(c)(1) of the Child Nutrition and WIC Reauthorization Act of 2004, P.L. 108-265, amends Section 17(f)(1)(C) of the Child Nutrition Act (CNA) by adding a new provision requiring State agencies to include in their State plans procedures for accepting and processing vendor applications outside the established timeframes if the State agency determines there will be inadequate participant access to the WIC Program. This includes instances in which a previously authorized vendor sells a store under circumstances that do not permit timely notification to the State agency of the change in ownership.

Implementation Date: This provision became effective October 1, 2004. State agencies must submit amendments to their fiscal year (FY) 2005 State Plans no later than May 1, 2005, to address this requirement.

Current Regulatory Requirement: Currently, Section 246.12(g)(7) of the WIC regulations requires the State agency to develop procedures for processing vendor applications outside of its timeframes when it determines there will be inadequate participant access unless additional vendors are authorized, and Section 246.4(a)(14) requires a description of the participant access criteria in the State Plan. Also, Section 246.12(h)(3)(xvii) provides the State agency the discretion to determine the length of advance notice required for vendors reporting changes in ownership. Thus all State Plans must currently describe participant access criteria, and many State Plans may also address vendor application processing timeframes.

Policy Change: The only change is the requirement for a State Plan amendment. The legislative provision reinforces the existing regulatory provisions by adding the requirement for a description of these procedures as part of the State Plan. State agencies which currently permit vendors to apply for WIC authorization without any restrictions on timeframes may continue to do so, although we suggest that these State agencies periodically evaluate whether such a policy results in effective vendor management and oversight.

PARTICIPANTS ALLOWED TO RECEIVE SUPPLEMENTAL FOODS FROM ANY AUTHORIZED VENDOR

Legislative Change: Section 203(c)(1)(A) of the Child Nutrition and WIC Reauthorization Act of 2004, P.L. 108-265, amends Section 17(f)(1)(C)(i) of the CNA to require WIC State agencies to allow participants to receive supplemental foods from any authorized vendor under retail food delivery systems.

Implementation Date: This provision became effective October 1, 2004. We recognize that system changes will be necessary. Therefore, State agencies must submit State Plan amendments no later than May 1, 2005, to reflect activities and target dates which will bring the State agency into compliance with this requirement no later than October 1, 2005.

Current Regulatory Requirement: None. Therefore, State agencies have been permitted to implement retail food delivery systems in which participants choose a specific authorized store at which to redeem their WIC food instruments.

Policy Change: State agencies are no longer allowed to operate retail food delivery systems that are "vendor-specific," i.e., that specify the vendor on the food instrument or otherwise require transaction of the food instrument at a designated vendor, even if the participant is provided an opportunity to choose the vendor to be designated. Therefore, State agencies must establish policy and revise systems to ensure that WIC participants are allowed to transact their food instruments at any retail store authorized by the State agency.

NOTIFICATION OF VENDOR VIOLATIONS

Legislative Change: Section 203(c)(5) of the Child Nutrition and WIC Reauthorization Act of 2004, P.L. 108-265, amends Section 17(f) of the CNA by adding a new paragraph (26) to require the State agency to notify the vendor of the initial violation, for violations requiring a pattern of occurrences in order to impose a sanction, prior to documenting another violation, unless the State agency determines that notifying the vendor would compromise an investigation.

Implementation Date: This requirement is effective for violations committed under investigations beginning on or after October 1, 2004.

Current Regulatory Requirement: Section 246.12(l)(3) of the WIC regulations provides that the State agency is not required to warn a vendor that violations had been detected before imposing a sanction.

Policy Change: This new legislative provision supersedes Section 246.12(l)(3). The State agency **must** notify a vendor in writing when an investigation reveals an initial violation for which a pattern of violations must be established in order to impose a sanction, before another such violation is documented, unless the State agency determines that notifying the vendor would compromise an investigation. This includes violations for a pattern of: overcharging; receiving, transacting and/or redeeming food instruments outside of authorized channels, including the use of an unauthorized vendor and/or an unauthorized person; charging for supplemental food not received by the participant; providing credit or non-food items, other than alcohol, alcoholic beverages, tobacco products, cash, firearms, ammunition, explosives, or controlled substances as defined in 21 U.S.C. 802, in exchange for food instruments; or providing unauthorized food items in exchange for food instruments, including charging for supplemental foods provided in excess of those listed on the food instrument. This notice requirement also applies to any violations for which a pattern of violations must be established in order to impose a State agency vendor sanction per Section 246.12(l)(2).

Notification is not required for violations involving a vendor's redemptions exceeding its inventories, since there are no initial violations in such instances. Additionally, such notice is not required for WIC vendor disqualifications or civil money penalties based on Food Stamp Program sanctions. Neither is notification required for violations that only require one incidence before a sanction is imposed.

Vendor agreements and sanction schedules need to be reviewed and amended as appropriate to reflect this new requirement.

As noted above, the State agency is not required to notify the vendor after the initial violation if the State agency determines that such notice would compromise an investigation. The notice could compromise an investigation if the investigation is covert, such as a compliance buy investigation, which involves an investigative agent posing as a WIC participant and transacting WIC food instruments. In such circumstances, the notice would reveal the existence of an investigation which had been previously unknown to the vendor.

The notice could compromise covert investigations of the vendor being conducted by the Food Stamp Program, the USDA Office of the Inspector General, the State Police, or other authorities, as well as the WIC investigation being conducted by the State agency; the term "investigation" does not exclusively refer to WIC investigations. Ideally, these other authorities should coordinate with the WIC State agency to prevent several investigations of the same vendor from being conducted at the same time. However, sometimes the WIC State agency may not learn about the existence of another investigation until after the WIC investigation has already begun.

The legislative provision provides the State agency with the discretion to consider such possibilities and use its judgment to determine whether a notice makes sense. Such determinations must be made on a case-by-case basis. In making this determination, there are a number of factors which the State agency may wish to review – for example, the severity of the initial violation, the compliance history of the vendor, or whether the vendor has been determined to be high risk consistent with Section 246.12(j)(3) of the WIC regulations. The State agency has the discretion to determine which factors to consider and how much weight should be assigned to each factor. If the State agency decides not to send the notice, the basis for this decision should be documented in the vendor file since the matter may be raised on appeal of any adverse actions taken as a result of the investigative activity.

LIST OF INFANT FORMULA WHOLESALERS, DISTRIBUTORS, RETAILERS, AND MANUFACTURERS

Legislative Change: Section 203(e)(8) of the Child Nutrition and WIC Reauthorization Act of 2004, P.L. 108-265, amends Section 17(h)(8)(A) of the CNA by requiring that each State agency: 1) maintain a list of infant formula wholesalers, distributors, and retailers licensed in the State in accordance with State law (including regulations), and infant formula manufacturers registered with the Food and Drug Administration (FDA) that provide infant formula; and 2) require authorized vendors to only purchase infant formula from sources on the above-described list.

Implementation Date: This requirement became effective October 1, 2004. State agencies must provide their vendors with these lists no later than May 1, 2005, which the vendors must begin to use for purchasing infant formula by October 1, 2005.

Current Regulatory Requirement: None.

Policy Change: This provision is intended to prevent stolen infant formula from being purchased with WIC food instruments. Such formula may constitute a health hazard. Health hazards from stolen infant formula include direct tampering with formula before it is sold to unsuspecting retailers, falsification of labeling to change expiration dates, counterfeiting, or improper storage.

State agencies are required to notify vendors that they must purchase infant formula only from the listed sources, since only such formula may be sold for WIC food instruments. State agencies may allow vendors to purchase infant formula from a supplier listed on another State agency's list. Further, State agencies need to amend their State Plans, vendor agreements, vendor manuals, and vendor training plans and materials to include these new requirements.

The State agency must also adopt a new vendor selection criterion requiring vendors to obtain infant formula from the listed sources as a condition of authorization. Adoption of a selection criterion must be consistent with the requirements of Section 246.12(g)(3), including a State Plan amendment, and revisions of vendor application instructions, vendor manuals, etc., to be consistent with the State Plan amendment. Additionally, the State agency may adopt a new vendor sanction for obtaining infant formula from an unlisted source; this is optional. If the State agency opts to do this, then the vendor sanction schedule, which is part of the vendor agreement, must be revised to include sanctions for violations of these requirements; such sanctions need to be consistent with Section 246.12(l)(2) of the WIC regulations, which cover State agency vendor sanctions. For the selection criterion to be effective, and for sanctions to be effective if a State agency chooses to also adopt sanctions, vendors must be required to maintain invoices or receipts showing the source of their infant formula purchases to enable the State agency to monitor vendor compliance.

As previously noted, the State agency must maintain a list of infant formula wholesalers, distributors, and retailers licensed in the State in accordance with State law (including regulations), and infant formula manufacturers registered with the FDA that provide infant formula. Thus the two sources for compiling this list would be: 1) the FDA; and, 2) the State authority for licensing and inspecting businesses selling food, involving either health licensing or business licensing. Also, the license or permit need not specify infant formula.

Further, this list should be provided to vendors on at least an annual basis, and vendors should also be provided with a phone number or e-mail address to inquire about a source which is not listed since it might have been licensed after the annual list was issued. Alternatively, the list could be maintained on line and frequently updated, although some vendors may not have Internet capability and will need a hard copy provided by the State agency.

IMPOSITION OF EBT COSTS ON VENDORS PROHIBITED

Legislative Change: Section 203(e)(11) of the Child Nutrition and WIC Reauthorization Act of 2004, P.L. 108-265, amends Section 17(h)(12) of the CNA by replacing it with a new provision which prohibits the Secretary from imposing or allowing a State agency to impose the cost of EBT equipment, systems, or processing on retail vendors as a condition for authorization or participation in the program.

Implementation Date: This provision became effective June 30, 2004.

Current Regulatory Requirement: None.

Policy Change: The new legislation prohibits the Department of Agriculture from imposing or allowing a State agency to impose EBT costs or *require* retail vendors to pay such costs as a condition for authorization or program participation. Such costs include EBT equipment, systems or processing which are directly attributable to a WIC EBT system and used solely for the WIC Program. Retailers may, however, continue to provide funding for WIC EBT on a voluntary basis, as a number of retailers have already done. Since WIC EBT is intended to improve program efficiency, retailers may make a business decision to share in the costs of WIC EBT.

EBT processing is the automated data processing in support of WIC EBT purchase transactions and the associated reimbursement to retailers for their daily WIC EBT business. These activities may be carried out by the State agency or a State agency's contracted EBT processor and/or payment processor.

It is customary practice for commercial processors that support retailer credit, debit and food stamp EBT transactions to charge processing fees. Banks also charge fees for automated credits to their customers' accounts. These types of processing fees result from specific retailer business decisions; and thus, if a retailer decides to participate in a State EBT system, this cost would not be imposed by the State agency, but would result in a cost to the retailer as a part of their commercial relationships.

Previously, Section 17(h)(12) of the Child Nutrition Act required the Secretary to submit a long-range plan for the development and implementation of WIC management information systems (including EBT). At that time, Congress prohibited State agencies from *requiring* retail stores to pay costs associated with WIC EBT until this report was submitted to Congress. The Secretary submitted the required report to Congress in March 2001.

RESTRICTIONS ON VENDOR INCENTIVE ITEMS

Legislative Change: Section 203(e)(13) of the Child Nutrition and WIC Reauthorization Act of 2004, P.L. 108-265, amends Section17(h)(14) of the CNA by prohibiting a State agency from authorizing or making payments to vendors, as described below, that provide incentive items or other free merchandise, except food or merchandise of nominal value (as determined by the Secretary), to program participants unless the vendor provides to the State agency proof that the vendor obtained the incentive items or merchandise at no cost.

The incentive item and free merchandise restriction applies to for-profit vendors:

(a) for which more than 50 percent of the annual revenue of the vendor from the sale of food items consists of revenue from the sale of supplemental foods that are obtained with food instruments; or
(b) who are new applicants likely to meet the criteria of item (a) under criteria approved by the Secretary.

These vendors are referred to below as vendors that meet the 50 percent criterion.

Implementation Date: This provision became effective October 1, 2004. This provision must be implemented by May 1, 2005.

Current Regulatory Requirement: None

Policy Change: This provision arose from concern regarding the wide array of incentive items offered by stores commonly known as WIC-only vendors to participants – including diapers, strollers, bicycles, small kitchen appliances, other household products, and sales or "specials" which increase WIC costs for supplemental food obtained with WIC food instruments. In addition, cash incentives are sometimes offered to participants who bring new customers to these stores. Because WIC-only vendors serve WIC participants exclusively or primarily, the stores' earnings necessarily flow from the WIC Program.

To ensure that the WIC Program does not pay the cost of incentive items in the form of high food prices, this provision prohibits giveaways of incentive items or other free merchandise by stores which meet the 50 percent criterion, unless the store can demonstrate that the items or merchandise were obtained at no cost. The law allows an exemption for food of nominal value or merchandise of nominal value, which FNS has defined as food or merchandise having a per item cost of less than $2. Even when allowing food or merchandise of nominal value, Congress directed that such items may not necessarily drive up WIC Program costs.

State agencies must approve all incentive items, if permitted at all, which vendors as described above intend to provide to WIC participants. Therefore, such vendors must submit to State agencies a list of incentive items, the cost of each item, and documentation, such as an invoice or similar document, indicating the costs of each incentive item. Documentation for items of greater than nominal value must indicate that the item was provided to the vendor at no cost. The WIC State agency may contact the source stated on the invoice or similar document to verify the information.

This memorandum also establishes policy to guard against circumvention of this provision by "selling" an incentive item to a WIC participant for less than it cost, e.g., "selling" a stroller to a WIC participant for $1 when the vendor paid $30 for the stroller. The vendor might believe that this sale is permissible since the incentive provision in the law refers to "free" food and merchandise provided by a vendor to a participant.

Vendors, as described above, must not be permitted to sell incentive items to participants below cost because the incentive items would most likely be purchased by the vendor with the proceeds of WIC purchases – i.e., with Federal funds – which the incentive provision seeks to prevent. Since such vendors must prove that an incentive item with greater than nominal value had been obtained at no cost, the vendor must also prove that an incentive item with greater than nominal value, and sold to a WIC participant, had been sold for no less than cost. Again, an invoice or similar document signed by the source of the items would be acceptable documentation.

Likewise, such invoices must be closely examined to ensure that the sources of the incentive items are not buying services or other arrangements designed to circumvent the law. For example, the vendor provides $30 to a buying service, which purchases a stroller for $30 and then either provides it to the vendor at no cost or for $1; the vendor then provides it to the participant at no cost or for $1. The State agency must ensure that the vendor does not provide this stroller to a WIC participant at no cost or for less than $30. As in the case of the previous example, this kind of arrangement would also circumvent the prohibition on using federal funds to provide incentive items above nominal value to participants.

In addition, due to the perceived value and unique nature of lottery tickets, vendors are not permitted to provide lottery tickets to participants for free or below the face value of the ticket. The law makes exceptions for merchandise or food of nominal value, but not for lottery tickets or the cash which may be won with a lottery ticket. Similarly, cash gifts to participants for any reason, such as bringing new customers to the store, are also prohibited. Merchandise or food items involved with a raffle or similar promotion are acceptable if obtained by the vendor at no cost or nominal cost, subject to documentation.

Further, vendors, as described above, are not permitted to provide services to participants such as transportation of participants to and from the vendor's premises, or delivery of supplemental food to participant residences, since such services would, in effect, be subsidized with Federal WIC funds. Such services are not permitted regardless of whether such services are of only nominal value. The only exception would be minimal customary courtesies of the retail food trade, such as bagging supplemental food for the participant and assisting the participant with loading the supplemental food into his/her automobile.

Finally, sales and "specials" for supplemental foods obtained with WIC food instruments are acceptable if certain conditions are met. Sales and specials include reduced prices for a period of time; buy one, get one free; buy one, get one at a reduced price; free amounts added to an item by a manufacturer; manufacturer coupons; and, store loyalty shopping cards. Sales and specials for supplemental foods obtained with WIC food instruments are acceptable if such sales or specials: 1) involve no cost or only a nominal value for the vendor regarding the food items involved; and, 2) do

not result in charging any amount to the WIC food instrument for more food than allowed for that food instrument.

As an example of the first condition, regarding buy one, get one free, the free food item would be acceptable if it had been obtained by the vendor at no cost or nominal cost, or if the vendor would be compensated for the second item, e.g., upon presentation of a manufacturer's coupon to the manufacturer. However, if the vendor had purchased the food item for $2 or more, then the free item would not be acceptable.

As an example of the second condition, regarding buy one, get one at a reduced price promotions, the reduced price may not be charged to the WIC food instrument if the second product is not covered by the food instrument; the WIC customer must pay this amount with his/her own money. Otherwise, this incentive item would be purchased with Federal funds, which is forbidden by the reauthorization law regarding vendors, as described above. Also, use of the food instrument to purchase a second product not covered by the food instrument would constitute a violation of Section 246.12(l)(1)(iv) of the WIC regulations, which mandates a one-year disqualification of the vendor for providing foods in excess of those listed on the food instrument. Moreover, as discussed previously, the vendor would not be allowed to "sell" the reduced-price item to the participant below cost, e.g., selling the item to the participant for $1.99 when the item had been purchased by the vendor for $10.

In summary, there are three types of acceptable incentive items:
1) merchandise obtained at no cost to the vendor and provided to participants without charge, or sold to participants at or above cost, subject to documentation;
2) food of nominal value and merchandise of nominal value, i.e., having a per item cost of less than $2; and,
3) food sales and specials which involve no cost or only a nominal value for the vendor regarding the food items involved and do not result in a charge to a WIC food instrument for foods in excess of the foods listed on the food instrument.

In addition to the other program objectives noted above, incentive items must also be consistent with WIC policy on the WIC acronym and logo. USDA has registered the WIC acronym and logo as trademarks with the U.S. Patent and Trademark Office. Under FNS Instruction 800-2, *WIC Program – Use of WIC Acronym and Logo,* June 2, 1992, the WIC acronym and logo must not be used on these incentive items, since this would suggest that the vendor is endorsed by, preferred by, or operated by the WIC Program. This prohibition on the use of the WIC acronym and logo applies to incentive items regardless of cost.

State agencies also need to revise their vendor authorization criteria and sanction schedules no later than May 1, 2005, to: 1) establish authorization selection criteria requiring vendors that meet the 50 percent criterion to abide by the restrictions on incentive items, and 2) establish sanctions for violations related to the restrictions on incentive items. Such sanctions must be consistent with the requirements of Section 246.12(l)(2) of the WIC regulations concerning State agency vendor sanctions. Likewise, sanctions should be consistent with FNS Instruction 800-2, *WIC Program – Use of WIC Acronym and Logo*.

VENDOR ADVISORY PANELS

During deliberations on P.L. 108-265 both the House and Senate expressed the benefits of maintaining a process of ongoing dialogue and collaboration between State agencies, authorized WIC vendors, representatives of retailer associations, and other entities interested in vendor management activities. Vendor advisory panels can be an effective mechanism for strengthening ongoing communication and collaboration between State agencies and the retail vendor community that provides supplemental foods. A number of State agencies have already established vendor advisory panels or boards as a means of obtaining input into the development and implementation of effective vendor management policies and procedures. Accordingly, State agencies are strongly encouraged to establish such vendor advisory panels if they have not already done so.